A STUDY IN THE DEVELOPMENT OF CREDITORS' RIGHTS.

III.

The conclusion to which our discussion has led us is that the only way to secure equality of distribution is to devise some method of procedure that will do two things:—(1) Bring the debtor's property into the court as a fund for equal distribution, and (2) By means of suit for the equal benefit of all the creditors, increase this fund with property which the debtor had previously transferred in breach of his obligation to hold his assets for equal distribution. That was our quest, and we followed it among the powers of chancery as revealed to us in its practice, for obviously the common law was a barren field of research. We found that there was a certain winding-up jurisdiction in chancery, but its limits were very narrow. The chancery court could distribute the estate of a deceased debtor; but what of a living debtor who stays at home and defies his creditors, or flees the country and leaves his goods to be done with as one may? Any such situation was beyond the court's jurisdiction.

Said one of our courts at an early date:[1]

"I have not been able to find any case where the mere absence of the debtor from the country, has been held to give a court of equity jurisdiction, independent of statute provisions, and according to the general rule on the subject, if the matter was cognizable in equity, but the defendant was not within the jurisdiction of the court, no suit could be entertained, or relief afforded. See Mitford's Pl. 30, note a. To remedy this defect, various statutes have been passed, in the several States of the Union, and also in England; and it is by virtue of these statutes, that courts of equity proceed against absent defendants, who are necessary parties to the bill, even where the subject-matter is of a pure equitable nature. And if a court of equity must look to statute aid, to enable it to proceed against an absent defendant, when the subject-matter is properly within the jurisdiction of a court of equity, it would follow, that the mere absence of a defendant from the jurisdiction, could not enable a court of equity to take jurisdiction of a matter of pure legal cognizance, as the collection of a simple contract debt."

In our country equity courts habitually wind up the affairs of corporations, but what of individual traders and unlimited partnerships? And finally, in sound logic, no reason can be found for the

[1]Sanders & McLaughlin *v.* Watson (1848) 14 Ala. 198.

extension of this winding-up jurisdiction beyond property which the debtor has actually on hand; there is no way, in strict reason, by which property fraudulently transferred can be restored to the estate for final distribution.

Thus at last we reach the bounds of the courts' powers, and must look elsewhere for the remedy. But we need not look far. The remedy lies near at hand in the shape of legislation, of so ancient an origin as to be a part of the body of the law in every sense, and a commonplace of every day thought. We refer to the various statutes on the subject of bankruptcy and insolvency. Insofar as mere information is concerned we might halt there; but if the rights of creditors are a subject worth studying at all, it will not do to stop an inquiry into their nature with a mere reference to existing legislation. For this legislation in its modern form is complex, and its history contains much that is fascinating. Here we are at the point where not only the common law, but the jurisdiction of equity itself, breaks down, yet complete relief is afforded by legislation of a far more ancient origin than some of the basic doctrines of equity. Sir George Jessel reminds us that we know the names of the chancellors who invented many of these doctrines, but no one knows the names of the men who first gave us, through Parliamentary enactment, a new body of law in the form of bankruptcy legislation. "It is obvious," says Fry, J.,[2] referring to the Statute of Fraudulent Conveyances, "that the intent of the statute is not to provide equal distribution of the estates of debtors among their creditors; there are other statutes which have that object." It is with these statutes that we propose now to deal, but necessarily in a most limited way, and only with reference to their primary feature of securing equality of distribution by means of creating a representative of the creditors and clothing him with rights exceeding their own.

Twenty-eight years before the Statutes of Fraudulent Conveyances, the first bankrupt act was introduced into the jurisprudence of England.[3] From a practical standpoint, however, bankruptcy legislation really commenced in the same year as the Statute of Fraudulent Conveyances, because in that year, 1570, was also enacted an act nominally amending, but really superseding, the Statute of Henry.[4] In the following reign the Elizabethan Act was

[2] *In re* Johnson (1881) L. R. 20 Ch. Div. 389, 392.

[3] (1542) Stat. 34-35 Hen. VIII, c. 4.

[4] Stat. 13 Eliz. c. 7.

much extended by two statutes;[5] and these three acts for two centuries formed the basis of all subsequent bankruptcy law. During succeeding years many changes were made, and notable indeed were those introduced by Sir Samuel Romilly's Acts;[6] but, until a general revision was made in 1824,[7] the statutes of Elizabeth and James formed the foundation of the English system of bankruptcy,[8] and for the purposes of our discussion we need not go much further than the state of the bankrupt laws at the time Lord Eldon took the Great Seal, because on that model was framed our own system, however more complex in the nature of things it may be.

Nothing is more characteristic of the method by which our law grows than this legislation; in working out a system of real justice under it, says Eden,[9] "the courts were driven into innumerable anomalies." Its original object was not so much to relieve the creditors from an intolerable situation, as to punish the bankrupt for putting them there; insolvency of the debtor was not so much the actuating cause of the commission as the debtor's having done something to hinder his creditors in realizing their claims. The acts of bankruptcy prescribed by the Statute of Elizabeth and James, and the vindictive punishments provided for the bankrupt, show this only too well. Therefore, the Statutes contemplated that the Chancellor, to whom this jurisdiction was committed,—a most fortunate omen of progress,—could act of his own motion in declaring a man bankrupt; but the reader can imagine the result so long as an English-bred lawyer should preside in that forum. "*Ex cautela,*" says Baron Comyn,[10] "the chancellor, before the commission is granted, usually requires a petition of the creditors, and an affidavit that they believe him to be a bankrupt." But while this extreme idea of state control was not suffered to have place, traces of these original conceptions still appear here and there. The courts naturally smelt fraud in the bankruptcy, rather than insolvency and misfortune, and so they suspected any attempt by the bankrupt to distribute his property among his cred-

[5]Stat. 1 Jac. I, c. 15; Stat. 21 Jac. I, c. 19.

[6]Stat. 46 Geo. III, c. 135; Stat. 49 Geo. III, c. 121.

[7]Stat. 6 Geo. IV, c. 16.

[8]Compare the treatment of the law in Cooke, Bankrupt Laws (4th ed.) London, 1799; and 1 Comyn's Dig. (1780) *s. v.* Bankrupt, with the preface to Eden, Bankruptcy, published after the enactment of the Revising Act of 1824.

[9]Eden, Bankr. 12.

[10]1 Comyn's Dig., *s. v.* Bankrupt, D. 1.

itors; hence the rule soon became fixed that a general assignment for the benefit of creditors was in itself a fraud on the bankrupt act.[11] As a result, when the Statutes made the general assignment an act of bankruptcy, it was held to justify an adjudication, and does to this day, entirely irrespective of whether or not the bankrupt was actually insolvent at the time he was so ill-advised as to try to save the expense of a bankruptcy.[12]

But the courts did not carry everything to such extremes; the saving grace of the common law, moderation, guided them in all points of real importance. Thus, the very common sense of the thing made the courts, however illogically, hold that a creditor who had participated in a general assignment was estopped from filing a bankruptcy petition founded thereon.[13] Through all such inconsistencies, and by means of being inconsistent, progress has steadily been made toward rendering the bankrupt law "a system for the regulation of mercantile insolvency"[14] such as it is today, and of necessity must be. It seems to be true, as an eminent judge has said,[15] that the bankruptcy system is "an example of what most of us have probably had occasion to note, that both the Parliaments and the Judges of those older times were bolder in initiative than their modern successors,"—certainly, this quality was essential if a new body of law was to be built.

We now reach the point of immediate interest to us, the creation of the creditors' representative and his powers. It was natural enough to create such a representative, because there had to be someone to care for the bankrupt's property until such time as a distribution could be effected. The bankrupt could not be left in the custody of this property for an instant, because originally bankruptcy was a proceeding *in invitum*. The bankrupt, according to the original conception, was a person to be punished for having reached the point of being unable to meet his debts, and for having committed acts which would frustrate the creditors' endeavor to reach payment of their debts by ordinary process of law. The Statutes therefore took from the bankrupt his property by force

[11]Small *v.* Oudley (1727) 2 P. Wms. *427; Kettle *v.* Hammond (1767) 1 Cooke, Bankr. L. 86; Stewart *v.* Moody (1835) 1 C. M. & R. 777; Barnes *v.* Rettew (C. C. 1871) 8 Phila. 133, Fed. Cas. No. 1019.

[12]West Co. *v.* Lea (1899) 174 U. S. 590.

[13]*Ex parte* Cawkwell (1812) 19 Ves. Jun. *233; Simonson *v.* Sinsheimer (C. C. A. 1899) 95 Fed. 948; *In re* Farthing (D. C. 1913) 202 Fed. 557; see also Boese *v.* King (1882) 108 U. S. 379.

[14]Eden, Bankr. 12.

[15]Christian, L. J., in *In re* Hickey (1875) 10 I. R. Eq. 117, 129.

of law, and acted directly upon the legal title thereto, transferring it from the bankrupt to a person selected by the court. In the words of an ancient writer,[16] it was considered "that the bankrupt has been guilty of a fraud, and that he is therefore an improper person to be entrusted any more with the management of his own estate," and hence other persons are appointed "in the place of the bankrupt, to whom, for the safety of the creditors, the commissioners are to convey the bankrupt's effects." In thus taking the debtor's property, Parliament, even at that early day, overrode the cherished ideas of the common law concerning the nature of property, for not only the bankrupt's goods, but even his land and his choses-in-action passed.

The next thing was to force the creditors to come in and share the proceeds of the property on a basis of equality. Originally it was provided that creditors could come into the bankruptcy within four months after the adjudication, but on condition that they contributed to the expense of the commission.[17] This, together with the fact that no system then existed for the discharge of the bankrupt from even the debts thus proven against his estate, led to a most unfortunate doctrine of election. The creditor, it was considered, could stay out of the bankruptcy, and could sue the debtor and take him in body execution, or any goods he might have which were not in the hands of the assignee. This idea persisted even after the amending acts which allowed the debtor his discharge,[18] and was very long in dying. In 1732, an attempt was made to cover the difficulty by a statute,[19] which provided that all costs of the bankruptcy should be paid out of the estate, and that the debtor should be eloigned from any imprisonment under execution by showing his discharge. It was not, however, until Sir Samuel Romilly's Act,[20] that this doctrine of election actually became "an object of curious research instead of a fund from whence any practical knowledge was to be derived."[21]

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[16] 1 Cooke, Bankr. L. 283.

[17] Stat. 1 Jac. I, c. 15, § 4.

[18] The first of which was Stat. 4 Ann. c. 17.

[19] Stat. 5 Geo. II, c. 30.

[20] Stat. 49 Geo. III, c. 121, § 14, continued by Stat. 6 Geo. IV, c. 16, § 59.

[21] Eden, Bankr. 111. See *Re* Gallison (D. C. 1871) 2 Low. 72, Fed. Cas. No. 5203. At present the bankrupt courts have power to stay suits that are pending against the debtor; English Act of 1883, c. 10; American Act of 1898, § 11a; and in America even after such a suit has gone to judgment the bankrupt may have it vacated. Boynton *v.* Ball (1887) 121 U. S. 457; Hill *v.* Harding (1882) 107 U. S. 631.

The aim of the courts, then, in their task of working these Statutes into a practical system of law, was to divide all the debtor's assets among his creditors and make all the creditors come into the distribution. In the words of Lord Hardwicke,[22] the right of the honest bankrupt to a discharge should be fully commensurate with the right of the creditors to divide up his goods. To attain this end it is obvious that creditors should share fairly, and that no man should prove for more than his due, nor should he be paid more thereon than his neighbor. Hence, an early statute[23] provided that bond creditors could prove only for what was justly due them, without respect to the penalty named therein, even if judgment for that penalty had been recovered. In likewise the race of diligence, the scramble for priority, must be stopped; and here we reach a scene of progress not yet ended.

To start with, it is obvious that the race of diligence must perforce be checked by the passage of the debtor's affairs into the custody of the court. No liens may be gained after that has happened. So far as the assets on hand are concerned that was clear from the beginning, for the assignee takes the property in the condition it was in on the date of the act of bankruptcy, however secret that may have been. "The property shall be vested in the assignee by relation from the first act of bankruptcy, as to the avoidance of all mesne acts."[24] This harsh doctrine was softened in many respects, and in our times has been legislated into limbo; but it had this good result, that it cut off all liens which the diligent judgment creditor had acquired during the period between the act of bankruptcy and the adjudication, because an action at the suit of the assignee lay against the sheriff who levied under any such judgment.[25] Finally, Sir Samuel Romilly's Acts provided that executions should be valid, if levied over two months before the adjudication, and all levied within this period should likewise avail, if taken without notice of the act of bankruptcy.[26] These enactments, substantially followed in our earlier acts of 1800 and 1841, had important results. It was considered that the statutes meant, so far as was justly possible, to provide a clear *glacis* around the bankruptcy so as to reduce priorities and accomplish

[22] *Ex parte* Groome (1744) 1 Atk. *115.

[23] Stat. 21 Jac. I, c. 19, § 9.

[24] 1 Comyn's Dig., *s. v.* Bankrupt, D. 26.

[25] Smith *v.* Milles (1786) 1 T. R. 475; Cooper *v.* Chitty (1756) 1 Burr. 20.

[26] Stat. 46 Geo. III, c. 135, § 1; Stat. 49 Geo. III, c. 121 § 2. See Eden, Bankr. 203 *et seq.*

the system's aim. Each creditor must, so far as could be required, lay down his claim of priority and come in as a simple claimant. In the average case the pressure of creditors is followed by the debtor's bankruptcy within thirty to ninety days, or just as soon as the impatient creditors have time to bring suit and enter up their judgments thereon. Hence, by avoiding all judgments entered within such a period, a substantial levelling would be accomplished and there would be few priorities left. That was the idea, but the courts could not completely enforce it; instead, they levelled only those priorities that had been obtained "in contemplation of bankruptcy," or practically under such circumstances as to constitute a fraudulent execution under the Statute of Fraudulent Conveyances. Perhaps there was a difference in this respect, but it is hard to find.[27] To us of the present day the distinction is of little importance, because our present Act contains sections[28] which, as construed by the Supreme Court in *Wilson* v. *Nelson*,[29] automatically destroy all liens obtained through judicial proceedings, within four months prior to the adjudication, without regard to fraud, intent or anything else. This is indeed the "high-water mark" of bankruptcy legislation; the Act of 1867,[30] operated only on attachments, and the present English Acts are still read in the old light.[31]

But whatever the modern differences may be, this tendency toward a levelling of judicial liens bears directly on our immediate subject of inquiry. We have seen that the bankruptcy system creates a representative to receive the debtor's property, and he receives it of necessity in the same plight and condition that the bankrupt left it. The assignee can get no higher rights in an honest contract than the bankrupt; where the latter is bound, there also is the assignee bound. Of this general proposition no doubt has ever been expressed, but it has its limitations. If it were carried to the extreme, the assignee would be in the same position as an assignee for the benefit of creditors who, as we have seen, could take only what the debtor gave, and hence could not claim whatever the debtor had given to others, however fraudulently. But the courts never went to that extreme. On

[27]Morgan *v.* Brundrett (1833) 5 B. & Ad. 289; Buckingham *v.* McLean (1851) 13 How. 151; Wilson *v.* City Bank (1873) 17 Wall. 473.

[28]§§ 67f and 3a.

[29](1901) 183 U. S. 191.

[30]§ 14.

[31]See opinion of Hotchkiss, Referee, in *Re* Rung Furniture Co. (1903) 10 Am. B. R. 44; Collier, Bankr. (8th ed.) 74.

the contrary, it was in bankruptcy only that all the three classes of wrongs could be righted, and that through the medium of the assignee.

There was little difficulty in the case of reputed ownership, because an early bankrupt statute defined the wrong and vested the assignee with the title to goods thus situated.[32] To this day in England the entire law of reputed ownership is bound up in the law of bankruptcy and does not exist beyond that pale.[33] In America, the Bankrupt Act of 1800 contained the "reputed ownership clause,"[34] but it has never appeared in any later national law, nor was it ever a feature of any State's legislation. Hence such law of reputed ownership as we have must rest on the doctrine of estoppel,[35] and the creditor in any such case can assert the estoppel only when he has gained, by a judgment, the right to interfere with his debtor's property. With us, therefore, the law of reputed ownership must be dealt with in the same way as the law of fraudulent transfer, and requires no distinct treatment.

It is in connection with the law of fraudulent conveyance that we can best appreciate the status of the assignee as the representative of the creditors. It is settled law that he can recover for the benefit of the estate property which the bankrupt had fraudulently conveyed, and effect this recovery by means of a plenary suit. No court has ever doubted that, yet few have ever tried to explain it. Nowadays, explanation is unnecessary, because the modern acts[36] expressly vest the trustee with the title to all property fraudulently conveyed. But even when the statutes were silent the assignee had this right of recovery, yet no judge thought it necessary to say much about it. Undoubtedly, as said by Jessel, M. R.,[37] "the trustee in seeking to set aside a transaction as fraudulent under the Statute of Elizabeth, is claiming by a higher and better title than the bankrupt himself, for the bankrupt is a party to the fraud." Such descriptive matter, however, does not answer the question; whence comes this higher right? It is likewise illuminating that the trustee always gets out of the bankrupt's shoes when it comes to any transaction which he, the trustee, is em-

[32]Stat. 21 Jac. I, c. 19, § 11.

[33]Colonial Bank *v.* Whinney (1886) L. R. 11 A. C. 426; Act of 1883, § 44.

[34]See Sands *v.* Codwise (N. Y. 1808) 4 Johns. *536.

[35]Frelinghuysen *v.* Nugent (C. C. 1888) 36 Fed. 229.

[36]*E. g.* §§ 67 & 70 of our Act of 1898.

[37]*Ex parte* Butters (1880) L. R. 14 Ch. Div. 265.

powered to avoid,[38] and that the assignee "represents both the corporation and its creditors."[39] But that is no answer to our inquiry. Perhaps Lord Loughborough comes nearest to the point when he says that "assignees have all the equity the creditors have, and may impeach transactions which the bankrupt himself would be estopped from impeaching;"[40] but, so far as reason goes, we find our answer only in an ultimatum,—"assignees have frequently been allowed as creditors under the Statute of Fraudulent Conveyances without question."[41]

There is, however, a rational basis for all this. In working out what finally came to be its real purpose, equality of distribution, Parliament and the courts co-operated in discouraging the creditors from obtaining priorities by means of judgments. The fewer creditors without judgment, the better it was for an easy administration of each case. Yet it would not do to deprive creditors of their only means of righting the wrong inflicted upon them by a fraudulent conveyance, without providing, as part of the new dispensation, an effective substitute. The basic bankruptcy statute, as we have seen, was enacted in the same year as the Statute of Fraudulent Conveyances; the two laws were only two chapters apart on the Parliamentary roll, and obviously must be read together. What was more natural than to say that, as a fraudulent conveyance is, by the terms of chapter 5, "void, frustrate and of no effect" against creditors, and as chapter 7 vests the assignee with title to the bankrupt's property, this assignee is therefore vested with the title to the property fraudulently conveyed? Our present Bankrupt Act incorporates both chapters in one, but logically no real difference is made; certainly statutes of the same session have just as close a kinship. By a later statute,[42] a fraudulent transfer by means of a deed was made an act of bankruptcy; but this really added nothing to the law, because a fraudulent conveyance by any other method was equally open to the assignee's attack.[43] The doctrine must therefore be left on this broad basis, that the two statutes work together. It follows that

[38]Claridge *v.* Evans (1908) 137 Wis. 218; Carey *v.* Donohue (1913) 209 Fed. 328.

[39]Chubb *v.* Upton (1877) 95 U. S. 665.

[40]Anderson *v.* Maltby (1793) 2 Ves. Jun. 244.

[41]May, Fraud. Conv. *171.

[42]Stat. 21 Jac. I, c. 15, § 2.

[43]Martin *v.* Pewtress (1769) 4 Burr. 2477; Dutton *v.* Morrison (1810) 17 Ves. Jun. *194.

those cases in our country which hold that, although the present Bankrupt Act in its definition of a fraudulent conveyance[44] limits it to an act happening within four months prior to the bankruptcy, nevertheless the trustee may recover property fraudulently conveyed at an earlier period,[45] are correct, and those to the contrary[46] lack sound basis. The trustee should in such a case be allowed to sue under the re-enactment of the Statute of Fraudulent Conveyances as found in the laws of the State where the transaction occurred; in short the state law and the federal Bankrupt Act should be made to co-ordinate so as to avoid the conclusion that Congress, by enacting the Bankrupt Act, intended to suspend in the various States a fundamental law which, taken in connection with a bankrupt act, materially aids in securing equality of distribution.

There seems never to have been any difference of opinion between the common law and the chancery courts on this point. Technically, the chancellor, in the exercise of his bankruptcy functions, did not sit as an officer of the court of chancery; but he was the same man for all that, and it was not long before the distinction was of little importance. Moreover, the court of chancery, either by means of proceedings by petition in the bankruptcy or by bill filed by or against the assignee, was soon defining for the use of future generations the position of the assignee, laying it down that this officer took all that the bankrupt had in the way of assets, both legal and equitable, and, on the other hand, that he took this estate subject to all outstanding equities with respect to it.[47] From this it turned to the assignee's position with respect to property which had been fraudulently transferred, taking jurisdiction of bills filed by assignees to get in property out of their natural reach, or by claimants against property which the assignees, by self-help alone, had gathered in. It was really the volume of this kind of business, rather than of judgment creditors' suits, which justified the remark of Kenyon, M. R., that the court of chancery had co-ordinate jurisdiction with courts of law over matters affected by the Statute

[44] § 67.

[45] Manning *v.* Patterson (D. C. 1907) 156 Fed. 111; *Re* Toothaker Bros. (D. C. 1904) 128 Fed. 187; *In re* Schenck (D. C. 1902) 116 Fed. 554; Shark *v.* Fitzhugh (1905) 75 Ark. 562; Hunt *v.* Doyal (1907) 128 Ga. 416.

[46] Murphy *v.* Murphy & Co. (1904) 126 Ia. 57; *semble,* Thomas *v.* Roddy (N. Y. 1907) 122 App. Div. 851; Woods *v.* Klein (1909) 223 Pa. St. 256; *In re* Ceballos & Co. (D. C. 1908) 161 Fed. 445.

[47] As an early example, see Parker *v.* Dykes (1698) 1 Eq. Cas. Abr. 54. See also 6 Columbia Law Rev. 562 *et seq.*

of Fraudulent Conveyances.[48] In course of time, the assignees began to institute such actions in the courts of common law, particularly in the case of personal property; and no technical argument appears to have been made against their recovery, probably because bankruptcy was the only branch of law where the common law courts were on common ground with the court of chancery and, hence, both disposed to yield to its opinion, and able to follow it in the use of their own processes. The only limit, therefore, that the common law courts put upon such suits was that "a demand and refusal were necessary to maintain the action." This was only right, because the assignees "might either affirm or disaffirm the contract, and if they thought proper to disaffirm it, they ought to have demanded the goods, a refusal to deliver which would have been evidence of a conversion."[49]

So complete has been the acquiescence of the common law courts in the view that the bankruptcy assignee may recover property fraudulently conveyed, that in our country there is a distinct tendency to restrict him to his common law remedy. Thus, in Massachusetts[50] and New York,[51] the Courts refuse to tolerate suits in equity by an assignee whose object is merely the recapture of property fraudulently conveyed; there must be more than that in the case before equity will give aid. The federal courts have never taken this step, and equity still has concurrent jurisdiction within their halls;[52] but it would seem that, if they had it to do over again, the national courts would have drawn the same sort of dividing line.[53]

We might stop at this point, and regard as superfluous another line of reasoning which leads to the same result, were it not true that upon it rests also the modern bankruptcy doctrine which forbids preferences. Preferences are expressly avoided by our present Bankrupt Act,[54] as they are by the English Statute of our times;[55] but long before our Act of 1867 the law of preferences had be-

[48]Hobbs *v.* Hull (1788) 1 Cox Ch. 445; see also Pratt *v.* Curtis (D. C. 1871) Fed. Cas. No. 11375.

[49]Nixon *v.* Jenkins (1793) 2 H. Bl. 135; Young *v.* Billiter (1860) 8 H. L. C. 682.

[50]Pratt *v.* Wheeler (Mass. 1856) 6 Gray, 520; see Bigelow, Fraud. Conv. 467 n.

[51]Allen *v.* Gray (1911) 201 N. Y. 504.

[52]Wall *v.* Cox (C. C. A. 1900) 101 Fed. 403.

[53]Parker *v.* Black (C. C. A. 1907) 151 Fed. 18.

[54]§ 60.

[55]Act of 1883, § 48.

come established, as a result of Lord Mansfield's view of the policy of bankruptcy legislation. The Chief Justice considered that the primary end of such statutes would be defeated if the debtor, prior to his affairs being brought into court for administration, could with impunity place his property beyond its reach, or himself pay such creditors as he pleased. The courts had already mooted this topic in holding general assignments to be against the policy of the Bankrupt Act;[56] but it remained for Lord Mansfield to carry the doctrine to its logical result, that either a preference or a fraudulent conveyance was impliedly forbidden by the Statute, and hence the assignee was entitled to the property constituting the subject-matter. As to fraudulent conveyances, he first laid down this rule in *Martin* v. *Pewtress*,[57] saying that "a trader can't alter the property of goods, by a criminal fraudulent transaction to the prejudice of his creditors." Respecting preferences, he is reputed to have first expressed himself at *nisi prius* in *Kettle* v. *Hammond*,[58] and the King's Bench, with himself presiding, followed this with a series of striking decisions.[59] The same doctrine was applied by the Supreme Court of Massachusetts in a case arising under our National Bankrupt Act of 1800.[60] "If indeed it be true," said Sedgwick, J., "as it undoubtedly is, that every attempt to defeat the public law is fraudulent and void, it then follows that the delivery of property to a creditor, in contemplation of bankruptcy, is fraudulent, notwithstanding the delivery is made in satisfaction of a *bona fide* debt." That is the basis of the law of preference; and even when the statutes, as nowadays, expressly forbid them, the idea remains the same. Thus the Supreme Court, construing those provisions of the National Act of 1867 which undertook to forbid preferences, considered the act which they intended to forbid as one committed "to prevent the property from coming into the hands of the assignee in bankruptcy and from being distributed under the bankrupt law."[61] So, by one line of reasoning or an-

[56](1767) 1 Cooke, Bankr. L. 86.

[57](1769) 4 Burr. 2478.

[58]Reported in 1 Cooke, Bankr. 85.

[59]Alderson *v.* Temple (1768) 4 Burr. 2235; Worseley *v.* Demattos (1758) 1 Burr. 467; Rust *v.* Cooper (1777) 2 Cowp. 629; Hassells *v.* Simpson (1784) 3 Doug. 361.

[60]Locke *v.* Winning (1807) 3 Mass. 325.

[61]Gibson *v.* Warden (1871) 14 Wall. 244. In utter forgetfulness of all this, however, the Supreme Court of late years has swung around to the view that a preference is nothing but *malum prohibitum* in the strictest sense of the term. Coder *v.* Arts (1908) 213 U. S. 223; Van Iderstine *v.* Nat. Discount Co. (1912) 227 U. S. 575. But that cannot unmake history.

other, we reach the conclusion that the trustee in bankruptcy is the representative of the creditors' rights in every sense of the word; and by plenary suit, instead of ancillary proceedings, he may redress those wrongs for the benefit of all the creditors. It follows, that, if any statute confers additional rights on the creditors, the trustee will succeed to those rights. In view of this, the incoming of the recording acts should have caused no difficulty, but nevertheless they did, and it is necessary that we examine this trouble.

Briefly, towards the middle of the nineteenth century, both in England and our States, statutes were adopted making void as against creditors various transactions affecting the title to personal property when unaccompanied by change of possession, unless public record of the details were made. Obviously, such statutes stand on the same ground with the Statute of Fraudulent Conveyances: all are for the benefit of creditors, and none can be used by a creditor without a judgment.[62] In plain common sense, should not an assignee in bankruptcy succeed to the same right? At first, there was but one answer. In *Bingham* v. *Jordan*[63] it was held that an assignee was entitled to attack an unrecorded transfer, on the ground that the policy of these statutes was the same as that of the Statute of Fraudulent Conveyances, and that the assignee represented the creditors under the one as under the other. The same view was taken by the New York Court of Appeals in *Southard* v. *Benner.*[64]

Indeed, the trustee should be considered, not of course as a purchaser in any sense of the word, as Lord Hardwicke pointed out years ago in *Walker* v. *Burrows,*[65] but as "a creditor armed with an attachment or execution."[66] If we view the trustee in this light, we have no more difficulty with the recording acts than we had with the Statute of Fraudulent Conveyances. This is especially true when we remember that these recording acts had a common origin with the Statute of Fraudulent Conveyances. We may make this assertion on high authority, for Lord Blackburn tells us that under the common law doctrine founded on *Twyne's Case* there was only presumption of fraud in the case of a bill of sale unaccompanied by change of possession, and that it was to make

[62]Myer *v.* Car Co. (1880) 102 U. S. 1; Skilton *v.* Coddington (1906) 185 N. Y. 80.

[63](1861) 1 Allen, 373.

[64](1878) 72 N. Y. 424; Skilton *v.* Codington (1906) 185 N. Y. 80.

[65](1745) 1 Atk. 93.

[66]Zartman *v.* Bank of Waterloo (1907) 189 N. Y. 267.

this more certain, by requiring either delivery or notoriety, that the English Bill of Sales Act was passed.[67]

In spite of all these considerations the Supreme Court in *Yeatman* v. *Savings Institution*[68] held that an unfiled chattel mortgage was valid as against the trustee in bankruptcy, because he did not occupy the status of a judgment creditor. Thus the Supreme Court and the New York Court of Appeals came to differ radically. One held that the trustee in bankruptcy had all the rights of a judgment creditor, and consequently could attack anything which was by statute made void as against creditors. The other held that, while he had that status with regard to fraudulent conveyances and preferences, he did not have that status with regard to any state law beyond such a point. This difference of opinion still existed when the Act of 1867 was repealed, and it revived with the passage of the Act of 1898.

It was undoubtedly to remedy this defect that the present Bankrupt Act provides in § 67a that, "claims which for want of record or other reasons would not have been valid liens as against the claims of the creditors of the bankrupt, shall not be valid liens as against his estate," and also provides in § 70 (5) that the trustee shall be vested with the title to all property which, prior to the filing of the petition, could by any means have been transferred or which might have been levied upon and sold under judicial process against him.[69] Yet, notwithstanding these provisions, the Circuit Court of Appeals in the Second Circuit held that an unfiled chattel mortgage was valid as against the trustee, except in behalf of such creditors as might meanwhile have obtained judgment, because it was the intention of the statute that only judgment creditors should attack such transactions.[70] Then the New York Court of Appeals in *Skilton* v. *Codington*[71] repeated the view which it had expressed in *Southard* v. *Benner,*[72] that under the New York law the trustee in bankruptcy *did* occupy the position of a judgment creditor with regard to the recording acts; whereupon, the Circuit Court of Appeals took the same view.[73]

The law thus stood that a trustee in bankruptcy cannot attack

[67] Cookson *v.* Swire (1884) L. R. 9 A. C. 653.
[68] (1877) 95 U. S. 764.
[69] See 6 Columbia Law Rev. 562.
[70] *In re* N. Y. Economical Printing Co. (C. C. A. 1901) 110 Fed. 514.
[71] (1906) 185 N. Y. 80.
[72] (1878) 72 N. Y. 424.
[73] *In re* Gerstman (C. C. A. 1907) 157 Fed. 549.

a state recording act unless the state courts have decided that a trustee in bankruptcy occupies the position of a judgment creditor. The Supreme Court, so far as its decisions really bear on the precise point, seemed in accord with this view.[74]

This *impasse,* however, has been relieved by Congress. In 1910, § 47a of the Statute was amended so as to declare that the trustee, as to all property not in the custody of the court, is "vested with all the rights, remedies and powers of a judgment creditor holding an execution returned unsatisfied." As the Massachusetts court pointed out in *Denny* v. *Lincoln,*[75] the Massachusetts insolvency law contained such an express provision at the time *Bingham* v. *Jordan* was decided, but it really made no difference. It has now been determined that the present amendment, while not affecting a valid lien which need not be recorded,[76] does "vest in the trustee for the interest of the creditors the potential rights of the creditors of that class."[77] Thus the judicial errata are cured, and we are brought back to where we started, with all the creditors' rights, however conferred, fully vested in the bankruptcy trustee.

This system, one would think, should have become universal in its scope, however narrowly its application might originally have been restricted. In an exact sense, that was not its destiny, for bankruptcy as such was always jealously restricted to certain classes of the economic state. In a broader sense, however, and tested by the principle of representation which has already been discussed, the system has spread beyond the domain of bankruptcy by the name of bankruptcy. That was the case in England; that became the case in this country. There was always a certain dislike for the word bankruptcy, in part because of the quasi-criminal nature of the early statutes; but all men finally realized the necessity of a system of statutory distribution and representation.

With exceptions so modern as to be neglible for their effect upon American legislation, the English bankrupt acts were confined in application to persons engaged in commerce, or, as they were called, traders. The Statute of Henry VIII was not thus limited and did not thus confine itself, but, as has been said,[78] "it appears to have been so regarded in practice; for one of the first cares of the Statute of Elizabeth is to define the class of merchants

[74] See 6 Columbia Law Rev. 562.
[75] (Mass. 1847) 13 Metc. 200.
[76] *In re* East End Mantel Co. (D. C. 1913) 202 Fed. 275.
[77] *In re* Bazemore (D. C. 1911) 189 Fed. 236.
[78] Jenks, Short History of English Law, 383.

capable of being made bankrupt." The basic definition made in the first section of that Act continued through all the changes of later amendments, that a trader was one "using or exercising the trade of merchandise by way of bargaining, exchange, re-exchange, bartery, chevisance or otherwise, in gross or by retail, or seeking his or her trade of living." In later days it became necessary to widen this definition. For instance, by the Statute 21 James I, c. 19, § 2, scriveners were brought within the acts, as persons "using the trade or profession of a scrivener, receiving other men's moneys or estates into their trust or custody," and this led to bankers, through having taken up the trade of scriveners, being brought within the definition, together with brokers;[79] so that finally, as a result of these inclusions, the Revising Act of 1824 defines as a trader,[80] "all persons using the trade of merchandise by way of bargaining, exchange, bartering, commission, consignment or otherwise, in gross or by retail, and all persons who, either for themselves or as agents or factors for others, seek their living by buying or selling, or by buying or letting for hire, or by the workmanship of goods or commodities." Traces of this distinction, and of a certain favoritism displayed by the legislators in its application, survive with us to this day. While the Statute of George II brings in, as subject to the Bankrupt Act, bankers, brokers and factors, it carefully exempts "farmers, graziers and drovers." To this day, with us, farmers and persons engaged chiefly in tillage of the soil are exempt from involuntary bankruptcy; and it was not until 1910 that our act was amended so as to allow corporations, not chiefly engaged in mercantile pursuits, to be adjudged bankrupt.[81]

But while the name of bankruptcy was odious, its principle became attractive after the debtor's discharge was made a part of the system. The pressure of the common law led the debtor, who was not subject to the bankruptcy *regime* provided for traders, to press Parliament for relief of the same nature, though of another name. It may very well be that imprisonment for debt was unknown to ancient common law; but it was of little avail to a debtor to urge such a point, in view of the successive statutes which extended the writ of *capias* to actions upon debts as well as trespass, so that any creditor could levy his execution upon the debtor's body and keep the debtor in prison until the writ was satisfied by the payment of the adjudged amount. The imprisonment of the debtor for

[79]Stat. 5 Geo. II, c. 30, § 39; Eden, Bankr. 6.
[80]Stat. 6 Geo. IV. c. 16, § 1.
[81]See Act of 1898, § 4.

a short space constituted an act of bankruptcy, so that if the debtor came within the trading class, his other creditors could bring his affairs into the bankruptcy court for distribution; but if the prisoner was merely a "poor debtor," and not a trader, no such relief could be had. Finally, however, the well-known legislation for the relief of insolvent debtors began. Its origin was ancient, certainly as old as the bankrupt laws, but the first permanent statutes which established a court for the administration of the debtor's property, and appointed an assignee for its reception, were the famous Acts of 1813 and 1814.[82] In common with the bankrupt acts, these insolvency laws were revised in the following reign;[83] but even before that, to use the words of an American counsel speaking in 1817, the situation in England was that "a legal system of insolvency was established; and courts possessing a peculiar jurisdiction, clearly and practically contradistinguished from bankruptcy, decided cases of insolvency in one room of Guildhall, while commissioners of bankruptcy were deciding cases of bankruptcy in another."[84]

This dual system provided in effect a method of getting the debtor into a court empowered to redress the creditors' wrongs, as well as to distribute the property on hand. There were only two omissions. One was the corporation. It could neither be a bankrupt nor a poor debtor, because the original conception of the corporation allowed no room for its winding-up in a commercial sense, and all that Parliament ever concerned itself with was to keep the stockholders in the great incorporated monopolies from being considered as traders and thus subject to individual bankruptcy.[85] The potential danger of this omission, however, was not

[82]Stat. 53 Geo. III, c. 102, and Stat. 54 Geo. III, c. 23.

[83]Stat. 7 Geo. IV, c. 57.

[84]Mr. Hunter, *arguendo* in Sturges *v.* Crowninshield (1819) 4 Wheat. 122, 142. The succeeding Statute of 1838, 1-2 Vict. c. 110, § 59, forbade preferences, and vested in the assignee the title to the property thus transferred; and it was also held that the assignee could recover property which the debtor had fraudently conveyed. Doe *v.* Ball (1843) 11 M. & W. *531; Young *v.* Billiter (1860) 8 H. L. C. 682.

[85]Thus in the time of the Protectorate, a statute which recited that "divers noblemen, gentlemen and persons of quality, no ways brought up to trade or merchandise, do oftentimes put in great stocks of money into the East-India Company, or Guiney Company and the fishing trade," goes on to provide that such a person shall not be "reputed a merchant or trader within any statute or statutes for bankrupts;" Stat. 13-14 Car. II, c. 24, § 3; and after the establishment of the Bank of England, a series of acts were passed exempting its stockholders from adjudication in bankrutcy as traders. Stat. 7-8 Wm. III, c. 31; 8-9 Wm. III, c. 20; 5 Ann. c. 13. "There are several other acts containing the same clause upon incorporating trading companies." 1 Cooke, Bankr. L. 12.

of real importance, because, with the increased use of the corporation as an instrumentality of ordinary commerce, came the Companies Acts with their admirable winding-up provisions, so that in England at the present day the bankruptcy of corporations is entirely covered by a separate statutory system. The other omission was the deceased or lunatic debtor. Obviously, the insolvent laws could not apply when the prisoner died before taking their benefit; and the bankruptcy system found the same difficulty in dealing with the executor, because unless he continued to conduct the decedent's business pursuant to directions of the will,[86] or the decedent belonged to a bankrupt partnership,[87] he could not, *qua* the decedent's estate, be considered as a trader. The present English Act[88] allows the estate of a deceased debtor to be adjudged bankrupt, thus finishing legislation which commenced many years ago.[89] But our Act does not go so far; with us, on the death of the respondent prior to the adjudication, the proceedings perforce abate.[90] It is still an open question in England whether a lunatic debtor can be adjudged bankrupt;[91] with us it seems clear that he cannot be adjudged upon an act of bankruptcy committed while insane,[92] nor may he file a voluntary petition.[93] In all such excepted cases we must look to the administrative processes of other courts than those of bankruptcy.[94] Such then, is an outline of the English system of liquidation in its more or less final form.

To some extent, as will appear from the more or less parenthetical references that have already been made, that is also our system, allowing for the many complexities which always appear when the common law's American progress is examined.

Confronted by the same pressing needs and with the demands of the mercantile community just as insistent, our courts and leg-

[86] *Ex parte* Garland (1804) 10 Ves. Jun. 110; *Ex parte* Richardson (1818) 3 Madd. 138.

[87] *In re* Pierce (1900) 102 Fed. 977; *In re* Temple (D. C. 1876) Fed. Cas. No. 13825; Briswalter *v.* Long (C. C. 1881) 14 Fed. 153.

[88] § 125.

[89] See 14 Columbia Law Rev. 280, n. 4.

[90] Act of 1898, § 8.

[91] See cases displayed in Williams, Bankr. (8th ed.) 5.

[92] *In re* Ward (D. C. 1908) 161 Fed. 755.

[93] *In re* Stein & Co. (C. C. A. 1904) 127 Fed. 547, and cases cited. Whether he may be adjudged a bankrupt upon an act committed while sane is a more doubtful question. See *In re* Funk (D. C. 1900) 101 Fed. 244; and *In re* Murphy (D. C. 1874) Fed. Cas. No. 9946; *contra, In re* Weitzel (D. C. 1876) Fed. Cas. No. 17365; and *In re* Pratt (D. C. 1872) Fed. Cas. No. 11371.

[94] Shepardson's Appeal (1869) 36 Conn. 23.

islatures were forced to work with tools not already fashioned to their hands. There was, as we have seen, a prejudice in England against the application of the term bankrupt to a debtor. There was also a prejudice against the fraudulent methods by which many debtors who were bankrupts achieved their freedom.[95] The American Colonies, although always tempted to protect the local debtor against his foreign creditor, still attempted in some instances to enact fair bankruptcy laws; but the Privy Council seemed to frown upon these attempts. The Massachusetts Act of August 31, 1757 was met, on June 29, 1758, by the opposition of representative merchants of the principal English cities, the ground of objection being this:—

"Its operation being not confined to insolvency in person, but extended to debtors in general, it is in the nature of a bankrupt law which, although just and equitable in abstract principle, has always been found in execution to afford such opportunity for fraudulent practice that even in this country, where usually all creditors are resident upon the spot, it may be doubted whether the fair trader does not receive more detriment than benefit from such a law. But in a colony, where possibly a one-tenth part of the creditors reside, a bankrupt law has hitherto been deemed inadvisable on account of injustice to the other nine-tenths of the creditors residing in Great Britain."[96]

There were then, and always have been, in this country, men who believed in the necessity of a general system of bankruptcy.[97] On the other hand, there were and are many of us who prefer to deal with the problem from quite a different standpoint, such as in the past has found expression in "stay laws" which were not

[95]The recitals of a statute, 5 Geo. II, c. 30, indicate the prevalence of such practices. In Lewis *v.* Chase (1720) 1 P. Wms. *620, the bankrupt, in order to get the consent of a creditor to his discharge, gave him a bond for the amount of the debt, and Parker, L. C., held the bond was valid. Doubtless to overcome this case, which Lord Mansfield, in Trueman *v.* Fenton (1777) 2 Cowp. 544, declared "smelt of the certificate," this statute was adopted, which among other things forbade all such acts. § 11.

[96]Similar objections were made on June 6, 1763, to the approval of an act adopted by the Province of Virginia. I am indebted for this information, drawn from the unpublished records in London, to the notes of Mr. Elmer B. Russell, who is preparing his thesis, on the subject of colonial legislation as affected by the rulings of the Privy Council, for a Doctor's degree in this University.

[97]Thus Madison says in Federalist No. 41: "The power of establishing uniform laws of bankruptcy is so intimately connected with the regulation of commerce, and will prevent so many frauds where the parties or their property may lie, or be removed into, different States, that the expediency of it seems not likely to be drawn into question." And writing in 1889 at a time when there was no Federal Bankrupt Act in force, Mr. Woodrow Wilson in The State, p. 494, speaks of the need of a uniform national system.

merely a feature of colonial legislation, but have appeared in economic crises until a comparatively late day.[98] Even today at every session of Congress bills are introduced to repeal the present Act.[99]

As a result of this conflict of thought we have had no less than four successive national bankrupt acts; but, worse than that, we have had no less than four periods where this country was without a bankrupt act. Bearing in mind the peculiar nature of our Union, as a result of which a state bankruptcy act stops in its operations at the borders of the local court's jurisdiction and can operate only on property included therein,[100] we can imagine the difficulty of fairly distributing the assets of a debtor who has been compelled to disregard the fact that when, in the course of his business, he crosses an imaginary line, he is going into a foreign country so far as jurisdiction over his tangible property is concerned. That is bad enough, but aggravation is added when we attempt to unify the laws of the different States with regard to the administration of the affairs of an insolvent. If every State had an insolvency law like that of Massachusetts (upon whose model two of our bankrupt acts have been framed) there would be some comfort in the repeal of the national Act, however little may be the excuse for such a course since the statute has been shorn of the features which led to the repeal of the Act of 1867.[101] But there never was such uniformity in state legislation, as is apparent from a glance at a compilation which appeared for the convenience of practitioners after the repeal of the previous national Act.[102] In some States, the insolvent laws forbid preferences,[103] but that is not the case in all the States. In others, as New York and New Jersey, an excellent system for the winding-up of corporations exists, but that is not the case in all the States. In some States, statutes authorize any officer appointed by a court for the distribution of a

[98]See for instance the stay law, passed by the State of Georgia on Dec. 13, 1866, which was held to be unconstitutional in Aycock *v.* Martin (1867) 37 Ga. 124.

[99]See the report of the Committee on Commercial Law at the last session of the American Bar Association (Rep. Am. Bar Ass'n vol. 38, p. 478) where mention is made of three different bills introduced in the present Congress to repeal the Bankrupt Act.

[100]Baldwin *v.* Hale (1863) 1 Wall. 223.

[101]It is generally known that the ostensible ground for the repeal of the former act was the excessive allowances granted by many of the Federal courts to receivers and counsel.

[102]R. J. Moses, Compilation of State Insolvency Laws (N. Y. 1879).

[103]See a list of these States in Bigelow, Fraud. Conv. 677 *et seq.*

debtor's assets, including the chancery receiver, the general assignee and the executor, to bring suit to set aside the debtor's fraudulent conveyances,[104] but such a statute is by no means a uniform model. Certainly it cannot be said that every State has always tried to protect foreign creditors as well as those near at home; in the teeth of the Constitution the legislature of one Commonwealth recently passed a law giving preferences in the distribution of the affairs of a domestic insolvent to his domestic creditors.[105]

But we must not let our indignation grow with our study of all this; on the contrary it should stimulate our interest and fortify our confidence that all will come out well in the end. For it is precisely out of conflicts, compromises and inconsistencies, that the whole law of creditors' rights has been generated; through conflict, compromise and inconsistency, will it continute to enlarge, in common with the general jurisprudence of a people who make their law as they really need it, rather than as it should be made.

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[104]See Mandeville *v.* Avery (1891) 124 N. Y. 376; Bate *v.* Graham (1854) 11 N. Y. 237.

[105]See Blake *v.* McClung (1898) 172 U. S. 239.